

China Natural Gas, Inc.
Form 10KSB/A
November 02, 2007

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

**FORM 10-KSB
Amendment No. 1**

**ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934**

For the fiscal year ended December 31, 2005

**TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934**

Commission File Number: 000-31539

CHINA NATURAL GAS, INC.

(Name of small business issuer in its charter)

Delaware
State or other jurisdiction of
incorporation or organization

98-0231607
I.R.S. Employer
Identification Number

Tang Xing Shu Ma Building, Suite 418
Tang Xing Road
Xian High Tech Area
Xian, Shaanxi Province
China

(Address of principal executive office)

Issuer's telephone number: 86-29-88323325

Securities registered under Section 12(b) of the Exchange Act: None

Securities registered under Section 12(g) of the Exchange Act: None

Check whether the Issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.) Yes No

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)
Yes No

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The Issuer's revenues for the year ending December 31, 2005 were \$4,850,699. As of March 17, 2006 the number of shares outstanding of the Issuer's common stock was 23,918,516.

As of March 17, 2006 the aggregate number of shares held by non-affiliates was approximately 15,227,500.

As of March 17, 2006 the aggregate market value of the Issuer's common stock held by non-affiliates was \$65,478,250, based on the average high and low price of \$4.30 per share as of March 17, 2006.

DOCUMENTS INCORPORATED BY REFERENCE None

EXPLANATORY STATEMENT

This Amendment No. 1 to Form 10-KSB, which amends the Company's Form 10-KSB for the year ended December 31, 2005, filed with the Securities and Exchange Commission (the "SEC") on March 22, 2006, is being filed to revise the disclosure regarding the Company's organizational history and the disclosure in Footnote 1 to the Company's Consolidated Financial Statements, in Item 1, Description of Business and in Item 6. Management's Discussion and Analysis or Plan of Operations to clarify that Xian Xilan Natural Gas Co. Ltd. is a 100% Variable Interest Entity of the Company, which financial results are consolidated with those of the Company's in accordance with Financial Interpretation No. 46R, Consolidation of Variable Interest Entities ("FIN 46R").

FORM 10-KSB**FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004**

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STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

In this annual report, references to "China Natural Gas," "CHNG," "the Company," "we," "us," and "our" refer to China Natural Gas, Inc.

Except for the historical information contained herein, some of the statements in this Report contain forward-looking statements that involve risks and uncertainties. These statements are found in the sections entitled "Business," "Management's Discussion and Analysis or Plan of Operation," and "Risk Factors." They include statements concerning: our business strategy; expectations of market and customer response; liquidity and capital expenditures; future sources of revenues; expansion of our proposed product line; and trends in industry activity generally. In some cases, you can identify forward-looking statements by words such as "may," "will," "should," "expect," "plan," "could," "anticipate," "intend," "believe," "estimate," "predict," "potential," "goal," or "continue" or similar terminology. These statements are only predictions and involve known and unknown risks, uncertainties and other factors, including, but not limited to, the risks outlined under "Risk Factors," that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. For example, assumptions that could cause actual results to vary materially from future results include, but are not limited to: our ability to successfully develop and market our products to customers; our ability to generate customer demand for our products in our target markets; the development of our target markets and market opportunities; our ability to manufacture suitable products at competitive cost; market pricing for our products and for competing products; the extent of increasing competition; technological developments in our target markets and the development of alternate, competing technologies in them; and sales of shares by existing shareholders. Although we believe that the expectations reflected in the forward looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Unless we are required to do so under US federal securities laws or other applicable laws, we do not intend to update or revise any forward-looking statements

PART I

ITEM 1. DESCRIPTION OF BUSINESS

Organizational History

We were incorporated in the state of Delaware on March 31, 1999, as Bullet Environmental Systems, Inc. On May 25, 2000 we changed our name to Liquidpure Corp. and on February 14, 2002 we changed our name to Coventure International, Inc.

On December 6, 2005, we issued an aggregate of 4 million shares to all of the registered shareholders of Xian Xilan Natural Gas Co., Ltd., and entered into exclusive arrangements with Xian Xilan Natural Gas Co., Ltd. and these shareholders that give us the ability to substantially influence Xian Xilan Natural Gas' daily operations and financial affairs, appoint its senior executives and approve all matters requiring shareholder approval. As a result, the Company consolidates the financial results of Xian Xilan Natural Gas as a variable interest entity pursuant to Financial Interpretation No. 46R, "Consolidation of Variable Interest Entities." On December 19, 2005, we changed our name to China Natural Gas, Inc.

Overview of Business

We primarily engage in the transmission and distribution of natural gas to commercial, industrial and residential customers. As well as the distribution of compressed natural gas as a vehicular fuel to retail end users.

Business

End User Delivery of Natural Gas

We are the sole authorized provider of natural gas to residential customers in certain parts of the Xian area, including Lantian County and the Baqiao District. We are currently supplying natural gas to approximately 50,000 households in the Xian area. Via a connecting point with a high pressure pipeline network from the government operated Shaanxi Natural Gas Company, natural gas with much lower pressure is delivered to our residential, commercial and industrial customers. We own approximately 120 km of high pressure pipeline. We are the only private company in Shaanxi province to own this type of high pressure pipeline.

Our management is seeking to expand supply services to the Shangluo and Ankang areas of Shaanxi province. Upon approval from the government, we would also have the exclusive right to provide natural gas to residential and commercial end users in those areas. In order to obtain such approval, we were required to submit a project proposal for the feasibility of supplying gas to each area. In Ankang, we applied to the Urban and Rural Construction Bureau. In Shangluo, applications were made to the Municipal Administration Bureau. The approval process takes approximately four to six months and is pending.

Wholesale to Filling Stations

We sell compressed natural gas to filling stations on a wholesale basis. The stations, in turn, sell natural gas to taxis and buses in Xian which operate on compressed natural gas (CNG) technology. Government statistics indicate that there are currently 5,000 buses and 20,000 taxis using natural gas in Xian. Each bus uses an average of 70 cubic meters of CNG per day and taxis use an average of 30 cubic meters of CNG per day (source: Xian Clean Fuel Vehicles Commission 2005).

In July 2005, we purchased a Compressor Station which is operated in proximity to our pipeline and which allows us to compress and transport natural gas via truck to retail gas stations. We also plan to develop a liquefied form of natural gas (LNG) that can be transported over longer distances by gas tanker truck and which could expand our geographical sales. We are currently conducting a feasibility study with regard to LNG production. This study should be completed in June 2006. In order to construct an appropriate LNG plant, we will require approximately US\$19 million (RMB 150 million), with construction of the plant completed by year end 2006, testing in October 2007 and production commencing in December 2007, assuming appropriate financing can be obtained. We can begin the process with our current licenses but in the future will require approval from Shaanxi Development and Reform Commission for LNG production.

Retail Filling Stations

Based on company estimates, by the end of June 2005, the total demand for compressed natural gas vehicular fuel in the Xian area was approximately one million cubic meters per day. We expect demand for natural gas as a transport fuel to continue to increase based on government clean energy policy as expressed in the proposal for the Eleventh Five Year Plan (2006-2010) and the end-user cost advantages of CNG fuel over gasoline. We estimate that the average filling station in Xian pumps approximately 12,000 cubic meters of natural gas per day. Based on a survey we conducted, as of November 1, 2005, there were 31 filling stations in Xian pumping approximately 372,000 cubic meters of CNG fuel per day, a figure well below estimated total demand.

As of February 9, 2006 we have completed construction and are operating two natural gas filling stations in the Xian metropolitan area. Currently, we purchase natural gas for 1.16 RMB/cubic meter and sell each cubic meter for 1.90RMB net of VAT. The construction time for each filling station is 45-60 days and the cost is approximately US\$600,000. As of March 17, 2006, we are in the process of constructing our third natural gas filling station. We continue to evaluate additional sites for natural gas filling stations in the Xian metropolitan area.

Our management believes that our vertically integrated operation should allow us to be able to surpass the average sales volume of competing stations, estimated at 12,000 cubic meters per day, based on our proprietary supply of CNG from our own pipeline.

Marketing

We market to the end user delivery of the natural gas segment of the business through advertising in the general media and direct solicitation of real estate development companies and government officials. We participate in trade shows and conferences such as the 7th Xian Global Gas Fuels Technology Equipment and Auto Service Station Exhibition which was held in June 2005. For the retail filling station segment of the business, we will target advertising to taxi drivers, who are the largest segment of end-users of the company's CNG fuel product. A discount loyalty card will be made available to the professional driving community including taxi and bus drivers. Brochures, radio and newspaper advertisements and point of sale displays will also be utilized.

Suppliers

Currently, we have only one natural gas supplier, the Shaanxi Natural Gas Co., Ltd., a government owned enterprise. In the past, contracts were renewed on an annual basis. However, as the volume of usage has increased, Shaanxi Natural Gas has revised their policies, and contract terms are now six months and subject to review prior to renewal. Our management reports that we do not expect any issues or difficulty in continuing to renew the supply contracts going forward. Price points for natural gas are strictly controlled by the government and have remained stable over the past 3 years.

Customers

Residential/Commercial

We supply natural gas to approximately 50,000 residential customers in Lantian County, Lintong and Baqiao Districts in the jurisdiction of Xian. These residences include apartment blocks and small estates. Commercial customers include small businesses like restaurants and office buildings.

Industrial

Within the Xian region there are several industries to which we supply natural gas as a raw material for their production process including the Xiwei Aluminum Company.

Wholesale to Filling Stations

Currently, we supply natural gas to several of the privately owned and operated CNG filling stations in the Xian area. Upon the completion of construction of our company-owned filling stations, we will also supply our own filling stations for sales to retail end users.

Industry Overview

China's rapidly expanding economy is stretching the limits of its energy resources. Currently, only 3% of China's total energy usage is natural gas, while the world's average consumption of natural gas is 24% of total energy usage. (source: US Energy Information Administration ("EIA"), August 2005) Over the next 5 years, China's use of natural gas is generally expected to double. China's domestic reserve of natural gas was estimated to be 53.3 trillion cubic feet (tcf) at the beginning of 2005 (source: EIA August 2005). The country's largest reserves are located in western and north central China, including the Province of Shaanxi, the home of CHNG.

In order to meet the growth in natural gas demand, the PRC government has encouraged private companies to invest in and build the natural gas infrastructure. On December 27, 2002, the Ministry of Construction issued a memorandum stating that regulation of the public utility industry (including gas distribution) should be liberalized and foreign and private investment participation should be encouraged and welcomed. The memorandum encouraged private investment in the sector and provided a legal framework for private urban natural gas distribution.

Intellectual Property

We have applied for a service mark on the "Xilan" name, which is used in connection with all services.

Research and Development

We have not had any material research and development expenses over the past two years. We project expenditures of approximately \$100,000 for research and development in 2006. The funding source for all research and development expenses is expected to come from operating cash flows.

Governmental and Environmental Regulation

To date, we have been compliant with all registrations and requirements for the issuance and maintenance of all licenses required by the applicable governing authorities in China. These licenses include:

- Qualified Urban Fuel Operator Business License authorized by the Shaanxi Construction Bureau, the local office of the Ministry of Construction, effective from January 2, 2004 to January 2, 2009.

(License number SHAANRANZHI 166)

- License to Supply, Install Equipment and Maintain Gas Fuel Lines issued by the local Gas Fuels for Heating Bureau, an agency of the Ministry of Construction and the Xian Natural Gas Management Bureau.

(License number: XIRAN 136)

- Safety and Inspection Regulation for Special Equipment Safety Inspection Standards for High Pressure Pipeline and Technical Safety Inspection Regulations from the Shaanxi Quality and Technology Inspection Bureau for compressor stations and pressure storage tank system. (Approval letter reference: 2004SHAANGUOCHUHAN033)
- Annual Safety Inspection of Lightning Conductor Equipment approved by the Shaanxi Meteorology Bureau. (Certificate number 0005274)

The Citygate and Compressor Stations are approved by the local office of the Ministry of Construction.

Fuel service station standards are subject to regulation by the Ministry of Construction, the General Administration of Quality Supervision, and the Bureau of Inspection and Quarantine of the People's Republic of China. Certificates will be issued upon satisfactory inspection of service stations.

There are various standards that must be met for filling stations including handling and storage of gas, tanker handling, and compressor operation. These standards are regulated by the Local Ministry of Construction and the Gas Field Operation Department of the Municipal Administration Committee. Inspections will be carried out by the Municipal Development and Reform Commission which will issue a certificate for the handling of dangerous chemical agents.

Standards for the design and construction of filling stations must conform to GB50156-2202 and technology standard BJJ84-2000.

Competition

The three largest state owned energy companies, CNPC (China National Petroleum Corporation) Group, SINOPEC, and CNOOC are principally engaged in the upstream supply of energy and are major players in exploration and transportation of oil and gas. They build much of the country's high pressure pipeline infrastructure. Natural gas is distributed to smaller regional firms that redistribute the gas to the end user, either through lower pressure pipeline networks, or via tankers in the form of liquid natural gas (LNG).

We are aware of two privately owned companies in China which may be considered to be our direct competitors: Xinjiang Guanghui LNG Development Corporation Ltd and Xin'Ao Gas Field Ltd. Xinjiang Guanghui LNG Development Corporation Ltd is primarily involved in the transportation of LNG via tanker truck to storage facilities from natural gas wells. Xin'Ao Gas Field Ltd. is a publicly owned company traded on the Hong Kong Exchange, distributing natural gas via pipeline, doing business in 13 provinces and municipalities that have a combined population of 31 million. Neither Xinjiang Guanghui nor Xin'Ao is approved to supply natural gas to any area in which Xilan is currently operating.

Currently, there are approximately 31 filling stations in Xian City. Thirteen of these stations are state owned enterprises. The other 18 stations are privately owned with the majority of these being single station operators. We believe that we can effectively compete with the stations based upon our organization, experience and financial resources.

Employees

As of March 17, 2006 we had a total of 243 employees in the following capacities: 6 in management; 16 in administrative; 87 in operations; 5 in sales department; 38 in R&D ; 16 in finance and 75 employees at the retailing filling station. We have not experienced any work stoppages and we consider relations with our employees to be good. We are not a party to any collective bargaining agreements.

ITEM 2. DESCRIPTION OF PROPERTY

Our principal executive offices are located at Tang Xing Shu Ma Building, Suite 418, Tang Xing Road, Xian High Tech Area, Xian, Shaanxi Province, China. Office #1 consists of approximately 137.9 square meters which are rented on a monthly basis for \$510.11 and office #2 consists of approximately 265.59 square meters which are rented on a monthly basis for \$982.45.

Our properties are located in Lantian county, Baqiao District and Gaoxin District of Xian, Shaanxi province. We own a 120km high-pressure underground pipeline network and two Citygate stations (terminals) with accompanying buildings and equipment. We lease the main office building where we are headquartered and three filling station sites.

We believe that current facilities are adequate for our current and immediately foreseeable operating needs. We do not have any policies regarding investments in real estate, securities or other forms of property.

ITEM 3. LEGAL PROCEEDINGS

From time to time, we may become involved in various lawsuits and legal proceedings, which arise in the ordinary course of business. However, litigation is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business. We are currently not aware of any such legal proceedings or claims that we believe will have, individually or in the aggregate, a material adverse affect on our business, financial condition or operating results.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITYHOLDERS.

None

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES.

On March 17, 2004, our common stock was approved for listing on the Over-the-Counter Bulletin Board under the symbol "CVNI" and on December 19, 2005 our symbol was changed to "CHNG" and our fiscal year end was changed to December 31. The following table sets forth, for the range of high and low closing bid quotations for our common stock since our common stock was listed on the Over-the-Counter Bulletin Board, reflecting the applicable fiscal periods based on the change in our fiscal year end. The quotations represent inter-dealer prices without retail markup, markdown or commission, and may not necessarily represent actual transactions.

Period	High*	Low*
December 31, 2005	\$ 3.60	\$ 0.5275
July 31, 2005	\$ 6.00	\$ 0.50
April 30, 2005	\$ 2.90	\$ 1.05
January 31, 2005	\$ 7.25	\$ 0.45
October 30, 2004	\$ 0.45	\$ 0.45
July 31, 2004	\$ 1.50	\$ 0.25
April 30, 2004	\$ 0.30	\$ 0.30

As of February 13, 2006, there were approximately 50 holders of record and 492 beneficial owners of our common stock.

Dividends

There are no restrictions in our articles of incorporation or bylaws that prevent us from declaring dividends. The Delaware General Corporation Law, however, does prohibit us from declaring dividends where, after giving effect to the distribution of the dividend:

1. We would not be able to pay our debts as they become due in the usual course of business; or
2. Our total assets would be less than the sum of our total liabilities plus the amount that would be needed to satisfy the rights of shareholders who have preferential rights superior to those receiving the distribution.

We have never declared or paid any cash dividends on our common stock. We currently intend to retain future earnings, if any, to finance the expansion of our business. As a result, we do not anticipate paying any cash dividends in the foreseeable future.

Recent Issuances of Unregistered Securities.

On January 17, 2006, the Company entered into securities purchase agreements with an accredited investor and completed the sale of \$2,824,802 of units. The units contained an aggregate of 1,008,857 shares of common stock and 274,633 common stock purchase warrants. Each common stock purchase warrant is exercisable for a period of three years at an exercise price of \$3.60 per share. Pursuant to the terms of the warrant, each investor has contractually agreed to restrict its ability to exercise the warrants to an amount which would not exceed the difference between the number of shares of common stock beneficially owned by the holder or issuable upon exercise of the warrant held by such holder and 9.9% of the outstanding shares of common stock of the Company.

On January 10, 2006 through January 13, 2006 the Company entered into securities purchase agreements with four accredited investors and completed the sale of \$2,195,198 of units. The units contained an aggregate of 783,999 shares of common stock and 213,422 common stock purchase warrants. Each common stock purchase warrant is exercisable for a period of three years at an exercise price of \$3.60 per share. Pursuant to the terms of the warrant, each investor has contractually agreed to restrict its ability to exercise the warrants to an amount which would not exceed the difference between the number of shares of common stock beneficially owned by the holder or issuable upon exercise of the warrant held by such holder and 9.9% of the outstanding shares of common stock of the Company. New York Global Securities acted as the placement agent of the transaction and received warrants to purchase 121,955 shares of common stock on the same terms and conditions as the investors.

On January 6, 2006 and January 9, 2006, the Company entered into securities purchase agreements with four accredited investors and completed the sale of \$5,380,000 of units. The units contained an aggregate of 1,921,572 shares of common stock and 523,055 common stock purchase warrants. Each common stock purchase warrant is exercisable for a period of three years at an exercise price of \$3.60 per share. Pursuant to the terms of the warrant, each investor has contractually agreed to restrict its ability to exercise the warrants to an amount which would not exceed the difference between the number of shares of common stock beneficially owned by the holder or issuable upon exercise of the warrant held by such holder and 9.9% of the outstanding shares of common stock of the Company. New York Global Securities acted as the placement agent of the transaction and received warrants to purchase 298,888 shares of common stock on the same terms and conditions as the investors.

* All of the above offerings and sales were deemed to be exempt under Section 4(2) of the Securities Act of 1933, as amended. No advertising or general solicitation was employed in offering the securities. The offerings and sales were made to a limited number of persons, all of whom were accredited investors, business associates of our company or executive officers of our company, and transfer was restricted by our company in accordance with the requirements of the Securities Act of 1933. In addition to representations by the above-referenced persons, we have made independent determinations that all of the above-referenced persons were accredited or sophisticated investors, and that they were capable of analyzing the merits and risks of their investment, and that they understood the speculative nature of their investment. Furthermore, all of the above-referenced persons were provided with access to our Securities and Exchange Commission filings.

Pursuant to a Share Purchase Agreement, which closed on December 6, 2005, we issued an aggregate 4,000,000 shares of common stock to former shareholders of Xian Xilan Natural Gas Co., Ltd. These shares were issued in reliance upon the exemption from registration provided by Regulation S under the Securities Act of 1933, as amended

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

INTRODUCTION

The following discussion should be read in conjunction with the Financial Statements and Notes thereto. Our fiscal year ends December 31. This document contains certain forward-looking statements including, among others, anticipated trends in our financial condition and results of operations and our business strategy. (See "Factors Which May Affect Future Results"). These forward-looking statements are based largely on our current expectations and are subject to a number of risks and uncertainties. Actual results could differ materially from these forward-looking statements. Important factors to consider in evaluating such forward-looking statements include (i) changes in external factors or in our internal budgeting process which might impact trends in our results of operations; (ii) unanticipated working capital or other cash requirements; (iii) changes in our business strategy or an inability to execute our strategy due to unanticipated changes in the industries in which the Company operates; and (iv) various competitive market factors that may prevent us from competing successfully in the marketplace.

Corporate History

We were incorporated in the state of Delaware on March 31, 1999, as Bullet Environmental Systems, Inc. On May 25, 2000 we changed our name to Liquidpure Corp. and on February 14, 2002 we changed our name to Coventure International, Inc.

On December 6, 2005, we issued an aggregate of 4 million shares to all of the registered shareholders of Xian Xilan Natural Gas Co., Ltd., and entered into exclusive arrangements with Xian Xilan Natural Gas Co., Ltd. and these shareholders that give us the ability to substantially influence Xian Xilan Natural Gas' daily operations and financial affairs, appoint its senior executives and approve all matters requiring shareholder approval. As a result, the Company consolidates the financial results of Xian Xilan Natural Gas as a variable interest entity pursuant to Financial

Interpretation No. 46R, "Consolidation of Variable Interest Entities." On December 19, 2005, we changed our name to China Natural Gas, Inc.

Critical Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and cash in time deposits, certificates of deposit and all highly liquid debt instruments with original maturities of three months or less.

Accounts and Other Receivable

We maintain reserves for potential credit losses on accounts receivable. We review the composition of accounts receivable and analyzes historical bad debts, customer concentrations, customer credit worthiness, current economic trends and changes in customer payment patterns to evaluate the adequacy of these reserves. Reserves are recorded primarily on a specific identification basis.

Inventory

Inventory is stated at the lower of cost, as determined on a first-in, first-out basis, or market. We compare the cost of inventories with the market value, and allowance is made for writing down the inventories to their market value, if lower. Inventory consists of material used in the construction of pipelines.

Property and Equipment

Property and equipment are stated at cost. Expenditures for maintenance and repairs are charged to earnings as incurred; additions, renewals and betterments are capitalized. When property and equipment are retired or otherwise disposed of, the related cost and accumulated depreciation are removed from the respective accounts, and any gain or loss is included in operations. Depreciation of property and equipment is provided using the straight-line method for substantially all assets with estimated lives as follo